

**STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION**

| | | |
|---|---|----------------|
| Charmar Water Company | : | |
| | : | |
| Proposed general increase in water rates | : | 11-0561 |
| (Tariffs filed June 29, 2011) | : | |
| | : | |
| Cherry Hill Water Company | : | |
| | : | 11-0562 |
| Proposed general increase in water rates | : | |
| (Tariffs filed June 29, 2011) | : | |
| | : | |
| Clarendon Water Company | : | |
| | : | 11-0563 |
| Proposed general increase in water rates | : | |
| (Tariffs filed June 29, 2011) | : | |
| | : | |
| Killarney Water Co. | : | |
| | : | 11-0564 |
| Proposed general increase in water rates | : | |
| (Tariffs filed June 29, 2011) | : | |
| | : | |
| Ferson Creek Utilities Company | : | |
| | : | |
| Proposed General Increase in Water and | : | |
| Sewer Rates | : | 11-0565 |
| (Tariffs filed June 29, 2011) | : | |
| | : | |
| Harbor Ridge Utilities, Inc. | : | |
| | : | 11-0566 |
| Proposed General Increase in Water and | : | (Cons.) |
| Sewer Rates | : | |
| (Tariffs filed June 29, 2011) | : | |

DRAFT ORDER

By the Commission:

I. Procedural History

On June 29, 2011, Charmar Water Company ("Charmar"), Cherry Hill Water Company ("Cherry Hill"), Clarendon Water Company ("Clarendon"), Killarney Water Co. ("Killarney"), Ferson Creek Utilities Company ("Ferson") and Harbor Ridge Utilities, Inc. ("Harbor") separately filed revised tariff sheets, hereinafter referred to as their "Filed Rate Schedule Sheets," in which they proposed a general increase in water and sewer

rates to be effective August 15, 2011. Charmar's tariff sheets were identified as Ill. C. C. No. 4, Sixth Revised Sheet No. 1, and Ill. C. C. No. 4, Second Sheet No. 1.1. Cherry Hill's tariff sheets were identified as Ill. C. C. No. 1, Thirteenth Revised Sheet No. 1, and Ill. C. C. No. 1, Third Revised Sheet No. 1.1. Clarendon's tariff sheets were identified as Ill. C. C. No. 3, Tenth Revised Sheet No. 1, and Ill. C. C. No. 3, Original Sheet No. 1.1. Killarney's tariff sheets were identified as Ill. C. C. No. 3, Ninth Revised Sheet No. 1, and Ill. C. C. No. 3, Original Sheet No. 1.1. Ferson's tariff sheets were identified as Ill. C. C. No. 1, Fourth Revised Sheet No. 1, and Ill. C. C. No. 1, Original Sheet No. 1.1. Harbor's tariff sheets were identified as Ill. C. C. No. 1 (sewer), Tenth Revised Sheet No. 1; Ill. C. C. No. 1 (water), Eighth Revised Sheet No. 1, and Ill. C. C. No. 1, Original Sheet No. 1.1.

On August 2, 2011, the Illinois Commerce Commission ("ICC" or the "Commission") entered Orders suspending the Filed Rate Schedule Sheets to and including November 27, 2011. On September 1, 2011, the Administrative Law Judge ("ALJ") granted a motion to consolidate the cases. On November 2, 2011, the Commission resuspended the Filed Rate Schedule Sheets to and including May 27, 2012.

Notices of the proposed increase in water and sewer rates were posted and published in a newspaper of general circulation throughout each of the Companies' service areas in accordance with the requirements of Section 9-201 of the Public Utilities Act ("Act") and with the provisions of 83 Ill. Adm. Code Sec. 255. Charmar, Cherry Hill, Clarendon, Killarney, Ferson and Harbor (collectively, the "Companies" or the "Utilities") also sent notice of the filing to customers in their first billings after the filing.

Leave to Intervene was granted to the Antioch Golf Club Community Association ("the Association") and the Illinois Attorney General ("Attorney General" or "AG") (collectively the "Intervenors").

Pursuant to notice as required by the law and the rules and regulations of the Commission, an evidentiary hearing was held before a duly authorized Administrative Law Judge ("ALJ") of the Commission at its offices in Chicago, Illinois, on January 25, and January 26, 2012. At the evidentiary hearing, the Utilities, Staff of the Commission ("Staff"), and the Attorney General appeared and presented testimony. The record was subsequently marked "Heard and Taken."

The Companies presented the following witnesses: Bruce Haas, Regional Director of Operations for the Midwest Region of Utilities, Inc. ("UI") and its subsidiaries, and Lena Georgiev, Regulatory Manager for the Atlantic and Midwest Regions of UI and its subsidiaries.

The following witnesses testified on behalf of Staff: Phillip Rukosuev, Cheri Harden and Christopher Boggs of the Rates Department, Financial Analysis Division; William R. Johnson, Thomas Q. Smith, William H. Atwood Jr. and Jonathan M. Sperry of

the Water Department, Financial Analysis Division; Theresa Ebrey and Dianna Hathhorn of the Accounting Department, Financial Analysis Division; David Sackett of the Policy Program, Energy Division and Janis Freetly of the Finance Department, Financial Analysis Division. The Attorney General offered the testimony of Michael L. Brosch, a consultant and accountant.

In their surrebuttal testimony, the Companies agreed to Staff's recommended revenue requirement as well as the accounting adjustments recommended in the direct and rebuttal testimony of the Staff witnesses. Staff and the Companies agree that Schedules that are described in and accompany ICC Staff Ex. _____, and the water and sewer rates identified in the Companies' Surrebuttal testimony should be adopted by the Commission.

On _____, 2012, the ALJ issued a Proposed Order in this matter. Briefs on Exceptions were filed by all of the parties on _____, 2012. Reply Briefs on Exceptions were filed by all of the parties on _____, 2012.

II. The Companies' Service Areas and the Nature of Operations

The Companies are wholly-owned subsidiaries of UI, which owns and operates water and/or wastewater systems throughout the United States. Water Service Corporation ("WSC") manages the operations for all of UI's water and sewer systems, including the Companies. WSC provides management, administration, engineering, accounting, billing, data processing, and regulatory services for the utility systems. WSC's expenses are assigned directly to an operating utility, or they are allocated to one or more of the various operating utilities, pursuant to a formula that has been approved by this Commission.

Charmar provides water service to approximately 53 customers in Lake County. Charmar's current water rate structure was approved pursuant to an Order, dated April 7, 2004, in Docket No. 03-0400. Cherry Hill provides water service to approximately 259 customers in Will County. Cherry Hill's current water rate structure was approved pursuant to an Order, dated April 7, 2004, in Docket No. 03-0401. Clarendon provides water service to approximately 363 customers in DuPage County. Clarendon's current water rate structure was approved pursuant to an Order, dated November 21, 1997, in Docket No. 97-0664. Killarney provides water service to approximately 346 customers in McHenry County. Killarney's current water rate structure was approved pursuant to an Order, dated May 24, 1995, in Docket No. 94-0329. Ferson provides water and sewer service to approximately 375 customers in Kane County. Ferson's current water and sewer rate structure was approved pursuant to an Order, dated June 21, 1984, in Docket No. 83-0432. Harbor provides water and sewer service to approximately 320 customers in Lake County. Harbor's current water and sewer rate structure was approved pursuant to an Order, dated October 23, 1995, in Docket No. 94-0512.

III. Test Year

The Companies' filings are based on a historical test year ending September 30, 2010, with *pro forma* adjustments for known and measurable changes. Neither Staff nor Intervenor challenged the reasonableness of using the year test year ending September 30, 2010 as a historical test year.

The Commission concludes that the test year ending September 30, 2010, with adjustments for known and measurable changes, is appropriate for the purposes of this proceeding.

IV. Rate Base

In their testimony, the Companies presented evidence showing their original cost rate bases after *pro forma* adjustments for the test year ending September 30, 2010. Staff proposed various adjustments to the Companies' rate bases including adjustments to utility plant, accumulated depreciation, and working capital. The Companies accepted all of the Staff's recommended rate base adjustments. The Attorney General, however, seeks additional adjustments.

A. Uncontested Issues

1. Plant Retirements

Staff witness Ebrey proposed adjustments for Cherry Hill, Clarendon, Killarney, Ferson Water and Ferson Sewer to reflect retirement of plant and annual depreciation expense related to retired plant that had not yet been removed from the utilities' books. The Companies accepted these adjustments. These adjustments are reasonable and are hereby approved.

2. Accumulated Depreciation

Staff witness Ebrey proposed adjustments to remove accumulated depreciation on previously retired plant. (Staff Ex. 2.0, pp. 13-15.) The Company accepted these adjustments. (Company Ex. 3.0, p. 7.) These adjustments are reasonable and are hereby approved.

3. Contributions in Aid of Construction ("CIAC")

Staff witness Ebrey proposed an adjustment to remove the effects of the amortization on CIAC which was not removed from the books of Harbor Sewer per the Order in Docket No. 94-0512. (Staff Ex. 2.0, p. 16.) The Company accepted this adjustment. (Company Ex. 3.0, p. 9.) This adjustment is reasonable and is hereby approved.

4. Pro Forma Plant Additions

Staff witness Ebrey proposed adjustments to update the pro forma plant additions for Cherry Hill, Killarney, and Harbor Water utilities based on responses to discovery, including revisions for Depreciation Expense and Accumulated Depreciation. (Staff Ex. 2.0, p. 16.) The Company accepted these adjustments. (Company Ex. 3.0, p. 8.) These adjustments are reasonable and are hereby approved.

5. Reclassification of Plant in Service

Staff witness Ebrey proposed adjustments to reclassify plant between the water and sewer utilities for Ferson and Harbor based on responses to discovery (Staff Ex. 2.0, pp. 16-17.) The Company accepted these adjustments and also reflected the accumulated depreciation effect of the reclassification. (Company Ex. 3.0, p. 8.) Staff accepted that additional adjustment. (Staff Ex. 10.0, p. 2.) .) These adjustments are reasonable and are hereby approved.

6. Accumulated Deferred Income Taxes

Staff witness Ebrey proposed adjustments to Accumulated Deferred Income Taxes resulting from the changes to depreciation expense resulting from other Staff adjustments. (Staff Ex. 2.0, p. 17.) The Company accepted these adjustments. (Co. Ex. 3.0, p. 9.) .) These adjustments are reasonable and are hereby approved.

7. Abandoned Charmar Plant

Staff witness Ebrey made the following proposals regarding Charmar Plant that was abandoned: 1) remove land easements and legal fees from plant in service that are associated with the abandoned plant; 2) correct the accumulated depreciation as well as the “extraordinary depreciation” associated with the abandoned plant; and 3) an amortization period of 15 years rather than 8.13 years as proposed by Charmar for recovery of the abandoned plant costs. Charmar accepted Staff’s adjustments in surrebuttal testimony.

Staff proposed adjustments to correct the Charmar’s calculation of accumulated depreciation and its proposed “extraordinary depreciation” associated with the abandoned plant as well as to address concerns related to: 1) estimated salvage and tax savings related to the property that was no longer being used that should be considered; 2) certain legal fees that were inappropriately included in plant accounts to be depreciated that should be removed; and 3) errors in the calculations that should be corrected. (Staff Ex. 2.0, pp. 7-10 and Staff Ex. 10.0, pp. 5-8.) The Charmar proposed an alternative methodology (Staff Ex. 10.0, p. 7) to Staff’s proposals for the computations of accumulated depreciation, which Staff accepted. (*Id.*, p. 8.) The Company accepted Staff’s adjustment for the Abandoned Charmar plant in surrebuttal testimony.

Staff proposed a 15-year amortization period for the costs of undepreciated plant (rather than the 8.13 years proposed by Charmar). (Staff Ex. 11-2.0, pp. 10-11.) Charmar accepted this proposal. (Staff Ex. 10.0, p. 8.) Staff witness Ebrey proposed that the retirement of the water treatment plant for Charmar be recorded according to the Uniform

System of Accounts Accounting Instruction 27(H) for the following reasons. First, the retirement was an unexpected retirement of a major unit of property, representing 37.12% of Charmar's proposed rate base. Second, this is an unexpected early retirement because over two-thirds of the treatment plant has been in service less than 10 years. Third, the recording of the retirement by crediting "plant in service" and debiting "accumulated depreciation" by the original cost of the investment being retired would cause a serious depletion in the depreciation reserve. If the cost of the treatment plant was debited to the depreciation reserve for the full cost it would cause that account's balance to become a debit balance twice the current credit balance. Thus, such an entry would cause a serious depletion to the reserve account. (Staff Ex. 2.0, pp. 11-13.) The Company accepted Staff's proposal for the accounting treatment of the retirement. (Company Ex. 3.0, p. 7.)

8. Depreciation Rates

With respect to depreciation rates, Clarendon, Killarney, Ferson and Harbor proposed moving from composite water and sewer depreciation rates to separate water and sewer depreciation rates for each primary account. Staff witness Johnson proposed some adjustments to the Companies' proposed water and sewer depreciation rates shown in ICC Staff Ex. 6.0, Schedules 6.01 KWC, 6.01 FCUC-W, 6.01 HRUI-W, 6.01 FCUC-S and 6.01 HRUI-S. The Companies agreed with Staff's proposed depreciation rate adjustments. These adjustments are reasonable and are hereby approved.

B. Contested Issues

1. Cash Working Capital Adjustment

For each utility, Staff witness Hathhorn proposed adjustments to working capital for the removal of real estate taxes and to incorporate the effects of other Staff-proposed adjustments to operating expenses. (Staff Ex. 1.0, pp. 7-8 and Sch. 1.08.) Staff accepted the Companies' calculations of their sewer and/or water working capital requirements using the 45-day or 1/8th formula method based on the operating expenses presented in their filings. The Companies agreed that these adjustments should be updated to reflect the operating expenses approved by the Commission. (Co. Ex. 3.0, p. 2.)

AG witness Mr. Michael Brosch proposed that a zero cash working capital ("CWC") allowance should be adopted, since the "Companies have not presented any reliable study to support an amount for CWC that should be included in rate base." (AG Ex. 1.0, pp. 21-22.) The Companies pointed out that a lead-lag study would be cost-prohibitive based upon the revenues it would expect to generate versus the increased cost to rate case expense. According to the Companies, the AG witness attempted to discredit the formula approach by selectively discussing only a few isolated expenses that fit his speculative belief that a full-blown lead-lag study might result in a zero or negative cash working capital allowance. Without an excessively expensive lead-lag study that looks at all expenses, the Companies argue it is impossible to show that the estimates produced by the formula method are unreasonable. Staff pointed out that the revenue

requirement impact of the Company's proposal in this case is very small; for example, for Charmar it is less than 1% of the revenue requirement recommended by Staff and the Companies. (*Id.*, at 276-277.)

The 45 day or 1/8th formula method has been accepted by the Commission for small water and wastewater utilities. See *Sundale Utilities, Inc.*, Ill. C. C. Doc. 08-0549 (Apr. 22, 2009); *New Landing Utility, Inc.*, Ill. C. C. Doc. 04-0610 (Jul. 19, 2005). The method has also been approved for a small gas and electric utility with about 7,000 customers. *Mt. Carmel Public Utility Company*, Ill. C. C. 07-0357 (Mar. 12, 2008). The lead-lag study preferred by the Attorney General would be cost-prohibitive based upon the speculative revenue savings it might generate versus the increased cost to rate case expense. The Commission finds the formula method provides a reasonable estimate of the cash working capital for the Companies, and the cash working capital requirements as adjusted by Staff should be included in rate base.

C. Commission Conclusion on Rate Bases

The Commission finds that Staff's adjustments to the Companies' rate bases are supported by the evidence, reasonable, and should be adopted. Upon giving effect to these adjustments, the Commission concludes that the rate bases approved for purposes of this proceeding are: \$295,125 for Charmar, \$498,213 for Cherry Hill, \$653,767 for Clarendon, \$603,588 for Killarney, \$632,085 (water) and \$631,969 (sewer) for Ferson, and \$451,925 (water) and \$65,159 (sewer) for Harbor. These rate bases maybe summarized as follows:

Charmar Approved Rate Base

| | |
|---|-----------------------------|
| | <u>Water</u> |
| Gross Plant in Service | \$332,986 |
| Less: Accumulated Depreciation and Amortization | <u>(\$10,003)</u> |
| Net Plant | \$332,983 |
| Additions to Rate Base | |
| Working Capital | \$5,180 |
| ADIT Regulatory Asset | \$0 |
| Adjustment to Rate Base Allocations | \$108 |
| Deductions from Rate Base | |
| Contributions in Aid of Construction | (\$836) |
| Accumulated Deferred Income Taxes | (\$32,310) |
| Customer Deposits | (\$0) |
| Rate Base | <u><u>\$295,125</u></u> |

Cherry Hill Approved Rate Base

| | |
|---|-------------------|
| | <u>Water</u> |
| Gross Plant in Service | \$411,133 |
| Less: Accumulated Depreciation and Amortization | <u>(\$77,986)</u> |
| Net Plant | \$333,147 |
| Additions to Rate Base | |
| Working Capital | \$9,108 |
| Net Pro Forma Plant | \$180,000 |
| Adjustments to Rate Base Allocations | \$527 |
| Deductions from Rate Base | |
| Contributions in Aid of Construction | (\$2,543) |
| Accumulated Deferred Income Taxes | (\$22,026) |
| Customer Deposits | (\$0) |
| Rate Base | <u>\$498,213</u> |

Clarendon Approved Rate Base

| | |
|---|------------------|
| | <u>Water</u> |
| Gross Plant in Service | \$750,671 |
| Less: Accumulated Depreciation and Amortization | <u>\$210</u> |
| Net Plant | \$750,881 |
| Additions to Rate Base | |
| Working Capital | \$15,625 |
| ADIT Regulatory Asset | \$0 |
| Adjustments to Rate Base Allocations | \$738 |
| Deductions from Rate Base | |
| Contributions in Aid of Construction | (\$28,519) |
| Accumulated Deferred Income Taxes | (\$84,958) |
| Customer Deposits | (\$0) |
| Rate Base | <u>\$653,767</u> |

Killarney Approved Rate Base

| | |
|---|--------------------|
| | <u>Water</u> |
| Gross Plant in Service | \$633,780 |
| Less: Accumulated Depreciation and Amortization | <u>(\$161,743)</u> |

| | |
|--------------------------------------|------------------|
| Net Plant | \$472,037 |
| Additions to Rate Base | |
| Working Capital | \$11,142 |
| Adjustment to Rate Base Allocations | \$705 |
| Net Pro forma plant | \$170,000 |
| Deductions from Rate Base | |
| Contributions in Aid of Construction | \$51 |
| Accumulated Deferred Income Taxes | (\$50,347) |
| Rate Base | <u>\$603,588</u> |

Ferson Approved Rate Base

| | <u>Water</u> | <u>Sewer</u> |
|---|--------------------|--------------------|
| Gross Plant in Service | \$1,383,047 | \$1,930,781 |
| Less: Accumulated Depreciation and Amortization | <u>(\$342,354)</u> | <u>(\$685,118)</u> |
| Net Plant | \$1,040,693 | \$1,245,663 |
| Additions to Rate Base | | |
| Working Capital | \$9,410 | \$15,320 |
| ADIT Regulatory Asset | \$0 | \$0 |
| Adjustments to Rate Base Allocations | \$764 | \$748 |
| Deductions from Rate Base | | |
| Contributions in Aid of Construction | (\$339,117) | (\$549,453) |
| Accumulated Deferred Income Taxes | (\$79,581) | (\$80,226) |
| Customer Deposits | (\$84) | (\$83) |
| Rate Base | <u>\$632,085</u> | <u>\$631,969</u> |

Harbor Approved Rate Base

| | <u>Water</u> | <u>Sewer</u> |
|---|--------------------|--------------------|
| Gross Plant in Service | \$963,019 | \$181,511 |
| Less: Accumulated Depreciation and Amortization | <u>(\$252,644)</u> | <u>(\$158,030)</u> |
| Net Plant | \$710,375 | \$23,481 |

| | | |
|--------------------------------------|------------------|-----------------|
| Additions to Rate Base | | |
| Working Capital | \$7,797 | \$6,145 |
| ADIT Regulatory Asset | \$0 | \$0\$0 |
| <u>Net Pro forma Plant</u> | <u>\$132,000</u> | <u>\$0</u> |
| Adjustment to Rate Base Allocations | \$650 | \$644 |
| Deductions from Rate Base | | |
| Contributions in Aid of Construction | (\$377,112) | \$56,433 |
| Accumulated Deferred Income Taxes | (\$21,785) | (\$21,544) |
| Rate Base | <u>\$451,925</u> | <u>\$65,159</u> |

Finally, Staff recommended that the Commission include the following provisions in this Order:

IT IS FURTHER ORDERED that the \$326,456 original cost of water plant in service for Charmar Water Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$402,961 original cost of water plant in service for Cherry Hill Water Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$702,376 original cost of water plant in service for Clarendon Water Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$627,242 original cost of water plant in service for Killarney Water Co. at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$1,335,221 original cost of water plant in service for Ferson Creek Utilities Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$1,910,182 original cost of sewer plant in service for Ferson Creek Utilities Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the sewer original costs of plant.

IT IS FURTHER ORDERED that the \$966,972 original cost of waterplant in service for Harbor Ridge Utilities, Inc. at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$199,135 original cost of sewer plant in service for Harbor Ridge Utilities, Inc. at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the sewer original costs of plant.

V. Operating Revenues, Expenses, and Income

The Companies presented their pro forma operating revenues, expenses, and income for the test year ended September 30, 2010. Staff proposed various adjustments to the Companies' pro forma operating statements. In addition, Staff made recommendations regarding tariff language changes and additional information to be provided by the Companies and UI's Illinois regulated utilities in future rate case direct testimony. Staff's proposed adjustments and recommendations are summarized below and reflected in Appendices A, B, C, _____ and _____. The Companies accepted all of Staff's recommendations and adjustments. The Attorney General, however, recommended additional adjustments.

A. Uncontested Issues

1. Add-On Tax Adjustment

Staff witness Hathhorn proposed adjustments to remove the Gross Revenue tax (also known as the Public Utility Fund tax) from the Companies' revenue requirements because it is not an actual operating expense of the utility and should not be included in tarified rates. Staff recommended that the Companies collect the tax as a separate charge on customers' bills when the rates approved in this docket go into effect. Ms. Hathhorn recommended the Companies add the following language should be added to their:

ANNUAL GROSS REVENUE TAX RECOVERY CHARGE

Section 9-222 of "The Public Utilities Act," as amended, authorizes a utility to recover from its Customers its liabilities to the State of Illinois for Public Utility Annual Gross Revenue Tax imposed by Section 2-202 of "The Public Utilities Act," as amended. Pursuant to Section 9-222, the Company shall charge an Additional Charge for the Public Utility Annual Gross Revenue Tax equal to 0.1% of all billings under this rate schedule except for (a) this Additional charge for Public Utility Annual Gross Revenue Tax, (b) the Additional Charge for any Municipal Utility Tax, and (c) any other

billings and billing items excluded from the base of the Public Utility Annual Gross Revenue Tax.

The Companies agreed with Staff's adjustment and recommended tariff language. This adjustment and recommendation are reasonable and are hereby approved.

2. CPI Increases

Staff witness Hathorn proposed an adjustment to disallow increases to test year expenses that are based on an inflation factor. Ms. Hathorn explained that pro forma adjustments to a historical test year should be based upon known and measurable changes. Inflation factors are not known and measurable. Accordingly, the Companies' pro forma adjustments for inflation should be disallowed pursuant to 83 Ill. Adm. Code 287.40 because the adjustments are based on the Consumer Price Index, which does not represent a specific study of known and measurable changes to the test year operating expenses. The Companies accepted Staff's adjustment. This adjustment is reasonable and is hereby approved.

3. Pro Forma Salaries and Benefits

For each utility, Staff witness Hathorn proposed adjustments to increase operating expenses to reflect the known and measurable costs of five additional personnel hired at Water Service Corporation ("WSC") hired after the WSC allocations of salaries and benefits to the test year were prepared. The Companies did not oppose the adjustments. This adjustment is reasonable and is hereby approved.

4. Legal Expense Normalization

For Charmar only, Staff witness Hathorn proposed an adjustment to decrease Charmar's legal expenses to reflect a more reasonable level expected to be incurred on an on-going basis. Chairman did not oppose the adjustment. This adjustment is reasonable and is hereby approved.

5. Unaccounted-for-Water

For Killarney only, Staff witness Hathorn proposed an adjustment to decrease Killarney's maintenance expenses because the unaccounted-for water percentage exceeded the maximum as defined in Killarney's tariff. Killarney did not oppose the adjustments. This adjustment is reasonable and is hereby approved.

6. Uncollectibles Expense

For Harbor only, Staff witness Hathorn proposed adjustments to decrease Harbor's uncollectibles expense at present rates to reflect the amounts at more reasonable levels expected to be incurred on an on-going basis. Harbor did not oppose the adjustments. This adjustment is reasonable and is hereby approved.

B. Contested Issues

1. Rate Case Expense

Staff witness Hathhorn proposed adjustments to operating expenses for each utility to: (1) increase the amortization period for rate case expense from three years to five years since it is a more reasonable estimate of the time period that rates from this proceeding would be in effect for these Companies; and (2) adjust the estimated travel expenses to more reasonable levels consistent with recent rate cases of affiliates of the Companies. In rebuttal testimony, the Companies updated their rate case expense estimate and revised proposed travel costs per Company in rate case expense. Staff agreed the updates provide a better estimate of the rate case expenses expected to be incurred than the costs in the Companies' direct case, and that the Companies' proposed reduced travel costs for rate case expense were a reasonable amount expected to be incurred for Company travel to the evidentiary hearing.

Staff further testified that Section 9-229 of the Act requires the Commission to expressly address in its final order the justness and reasonableness of any amount expended by a public utility to compensate attorneys or technical experts to prepare and litigate a general rate case filing. Therefore, Staff recommended that the Companies provide several of its data request responses for the record in these cases. The Companies agreed and provided exhibits in support of the justness and reasonableness of their rate case expense request. Based upon the evidence submitted by the Companies and reviewed by Staff, Staff further recommended that the Commission the amounts of compensation for attorneys and technical experts to prepare and litigate this proceeding, as adjusted by Staff, are just and reasonable pursuant to Section 9-229 of the Act, 220 ILCS 5/9-229.

AG witness Brosch testified that the Companies' method of inclusion of labor costs for WSC employees in rate case expenses results in consumers paying the same salaries twice: once through operating expenses and again through rate case expense recoveries. Staff disagreed with the AG and agreed with the Companies that the test year capitalized salary costs related to internal labor are deducted from the salary amounts in the test year, therefore, no double-counting occurs. Staff demonstrated line by line that there is no double-counting of internal labor in the test year. Staff explained that the Companies accomplish this by removing the costs of capitalized labor for capital projects from expenses, as well as the cost of employees' time working on rate cases outside of Illinois. Further, the WSC internal labor costs deferred for rate case recovery as detailed in Company Ex. 3.3 occurred post test year. Staff verified the Company's claim of no double counting of internal labor in rate case expense and test year labor charges. The Commission agrees with Staff and the Companies that the AG has failed to provide sufficient evidence to support its claim that any further adjustments to rate case expenses are warranted.

C. Commission Conclusion on Operating Revenues, Expenses, and Income

As discussed above, the Commission declines to adopt the adjustments recommended by the Attorney General and finds that the adjustments to operating revenues, expenses (including taxes) and utility operating income proposed by Staff are supported by the evidence, reasonable, and should be adopted. The operating income statements for the Companies for the test year ended September 30, 2010 are shown in Appendices A, _____, and _ and summarized below:

CHARMAR

Water

| | |
|--------------------------|-----------------|
| Operating Revenues | \$90,250 |
| Operating Expenses | <u>\$66,699</u> |
| Utility Operating Income | \$23,551 |
| Revenue Change | \$65,192 |

CHERRY HILL

Water

| | |
|--------------------------|------------------|
| Operating Revenues | \$169,812 |
| Operating Expenses | <u>\$130,055</u> |
| Utility Operating Income | \$39,757 |
| Revenue Change | \$84,284 |

CLARENDON

Water

| | |
|--------------------------|------------------|
| Operating Revenues | \$226,458 |
| Operating Expenses | <u>\$174,287</u> |
| Utility Operating Income | \$52,171 |
| Revenue Change | \$131,942 |

KILLARNEY

Water

| | |
|--------------------------|------------------|
| Operating Revenues | \$206,271 |
| Operating Expenses | <u>\$158,104</u> |
| Utility Operating Income | \$48,167 |

Revenue Change \$139,370

FERSON

Sewer

| | |
|--------------------------|------------------|
| Operating Revenues | \$234,582 |
| Operating Expenses | <u>\$184,152</u> |
| Utility Operating Income | \$50,430 |

Revenue Change \$101,803

Water

| | |
|--------------------------|------------------|
| Operating Revenues | \$180,666 |
| Operating Expenses | <u>\$130,226</u> |
| Utility Operating Income | \$50,440 |

Revenue Change \$81,951

HARBOR

Sewer

| | |
|--------------------------|-----------------|
| Operating Revenues | \$64,685 |
| Operating Expenses | <u>\$59,485</u> |
| Utility Operating Income | \$5,200 |

Revenue Change \$32,896

Water

| | |
|--------------------------|------------------|
| Operating Revenues | \$141,594 |
| Operating Expenses | <u>\$105,530</u> |
| Utility Operating Income | \$36,064 |

Revenue Change \$63,890

In addition, the Commission finds that the amounts of compensation for attorneys and technical experts to prepare and litigate this proceeding, as adjusted by Staff, are just and reasonable pursuant to Section 9-229 of the Public Utilities Act (220 ILCS 5/9-229); and the total unamortized rate case expense in the following amounts per Company are approved for recovery:

| | |
|--------------|-----------|
| Charmar | \$118,763 |
| Cherry Hill | \$115,807 |
| Clarendon | \$115,703 |
| Ferson Sewer | \$56,454 |
| Ferson Water | \$57,664 |
| Harbor Sewer | \$58,106 |
| Harbor Water | \$58,667 |
| Killarney | \$116,773 |

VI. Rate of Return

A. Capital Structure

Because the Companies are wholly owned subsidiaries of UI, Staff proposed using UI's capital structure for the year ending September 30, 2010. The capital structure is summarized below:

| <u>Component</u> | <u>Ratio</u> |
|------------------|--------------|
| Short term debt | 1.19% |
| Long term debt | 49.54% |
| Common Equity | 49.27% |
| Total | 100.00% |

B. Cost of Debt

Staff estimated that the Companies' cost of short-term debt is 3.08%. The Companies' embedded cost of long-term debt is 6.65%.

C. Cost of Common Equity

Staff recommended a 9.43% cost of common equity for the Companies. Staff measured the investor-required rate of return for UI with the discounted cash flow ("DCF") and risk premium models. DCF and risk premium models cannot be directly applied to UI because its stock is not market-traded. Therefore, Staff applied those models to water utility and public utility samples deemed comparable in risk to the Companies.

1. DCF Analysis

DCF analysis assumes that the market value of common stock equals the present value of the expected stream of future dividend payments to the holders of that stock. Since a DCF model incorporates time-sensitive valuation factors, it must correctly reflect the timing of the dividend payments that a stock price embodies. The companies in Staff's water and utility samples pay dividends quarterly. Staff therefore employed a non-constant-growth DCF ("NCD CF") model that reflects a quarterly frequency in dividend payments.

Staff used the NCD CF model in this proceeding because the level of growth indicated by the average 3-5 year growth rates for the Water and Utility samples is not sustainable over the long-term. The growth rate estimates were combined with the closing stock prices and dividend data as of September 29, 2011. Based on these growth assumptions, stock price, and dividend data, Staff's NCD CF estimate of the cost of common equity was 8.84% for the water sample and 9.25% for the utility sample.

2. Risk Premium Analysis

According to financial theory, the required rate of return for a given security equals the risk-free rate of return plus a risk premium associated with that security. Staff used a one-factor risk premium model, the Capital Asset Pricing Model ("CAPM"), to estimate the cost of common equity.

The CAPM requires the estimation of three parameters: beta, the risk-free rate, and the required rate of return on the market. For the beta parameter, Staff combined adjusted betas from Value Line, Zacks, and a regression analysis to estimate the beta of the water and utility sample. For the water sample, the average Value Line, Zacks, and regression beta estimates were 0.70, 0.57 and 0.54, respectively. For the utility sample, the average Value Line, Zacks, and regression beta estimates were 0.75, 0.77 and 0.72, respectively. The Value Line regression employs weekly observations of stock return data while both the regression beta and Zacks betas employ monthly observations. Since the Zacks beta estimate and the regression beta estimate are calculated using monthly data rather than weekly data (as Value Line uses), Staff averaged those results to avoid over-weighting betas estimated from monthly data in comparison to the weekly data-derived Value Line betas. Staff then averaged the resulting monthly beta with the Value Line weekly beta, which produced a beta of 0.63 for the water sample and 0.75 for the utility sample.

For the risk-free rate parameter, Staff considered the -0.01% yield on four-week U.S. Treasury bills and the 3.05% yield on thirty-year U.S. Treasury bonds. Both estimates were measured as of September 29, 2011. Forecasts of long-term inflation and the real risk-free rate imply that the long-term risk-free rate is between 4.3% and 5.5%. Staff concluded that the U.S. T-bond yield is currently the superior proxy for the long-term risk-free rate.

Finally, for the expected rate of return on the market parameter, Staff conducted a DCF analysis on the firms composing the S&P 500 Index. That analysis estimated that the expected rate of return on the market was 12.86% for the second quarter of 2011. Inputting those three parameters into the CAPM, Staff calculated a cost of common equity estimate of 9.23% for the water sample and 10.41% for the utility sample.

3. Staff Cost of Equity Recommendation

Staff estimated the investor-required rate of return on common equity for the two samples from the results of the NDCDF and risk premium analyses for the samples. The average investor required rate of return on common equity for the Water sample, 9.04%, is based on the average of the DCF-derived results (8.84%) and the risk premium-derived results (9.23%). The average investor required rate of return on common equity for the Utility sample, 9.83%, is based on the average of the DCF-derived results (9.25%) and the risk premium-derived results (10.41%). The investor required rate of return on common equity for the Companies, 9.43%, is based on the average for the water and utility samples

4. AG Cost of Equity Recommendation

The AG argued that the allowed return on common equity for the Companies should be reduced by no less than 100 basis points from the 9.43% agreed upon by Staff and the Companies to reflect the poor management shown by the high rate increases proposed and other consumer complaints. The Commission recently considered and rejected very similar arguments made by the AG in the recent consolidated rate cases (Ill.C.C. Doc. 11-0059/11-0141 and 11-0142 Consolidated) filed by three other Illinois water and sewer utilities owned by Utilities, Inc. The Attorney General failed to provide a cost of equity expert witness. As we noted in that proceeding, the Commission understands the concerns raised by the AG, and continues to find that the AG's recommendation is inconsistent with the reasonable standards by which the rate of return must be established.

5. Commission Analysis and Conclusions

Having reviewed the record, the Commission finds that the Companies should be authorized to earn a rate of return of 7.98% as recommended by Staff. The rate of return incorporates a return on common equity of 9.43%. The Companies' rate of return was derived as follows:

| <u>Source of capital</u> | <u>Amount</u> | <u>Percentage</u> | <u>Cost</u> | <u>Weighted Cost</u> |
|--------------------------|----------------------|-------------------|--------------|----------------------|
| Short-term debt | \$4,242,247 | 1.19% | 3.08% | 0.04% |
| Long-term debt | \$176,919,657 | 49.54% | 6.65% | 3.30% |
| Common Equity | <u>\$175,968,943</u> | <u>49.27%</u> | <u>9.43%</u> | <u>4.64%</u> |
| Total | \$357,130,846 | 100.00% | | 7.98% |

VII. Rate Design/Tariff Terms

A. Rate Design and Billing Cycle

Staff found the Companies' rate design proposals reasonable, but recommended the Commission set the rates based upon Staff's proposed revenue requirement, by multiplying the Companies' proposed customer and usage charges by the ratio of Staff's proposed revenue requirement to the Companies' proposed revenue requirement across-the-board.

The Commission finds the development and design of the rates in the manner recommended Staff are reasonable and should be accepted.

B. Miscellaneous

1. Miscellaneous Fees and Charges

Staff and the Companies agreed on all changes to the miscellaneous charges and tariff sheets. These changes are consistent with changes approved for other Utilities, Inc. companies in recent dockets and include: (Staff Ex. 4.0, pp. 22 – 43)

- NSF Check Charge increase to \$25;
- New Customer Charge increase to \$25;
- Reconnection Charge increase to \$37.50;
- Establish an After Hour Call-Out Charge at \$106 minimum;
- Establish an Annual Gross Revenue Tax equal to 0.1%;
- Ensure all Companies are on a monthly billing cycle;
- Ensure all Companies have a specific Bill Form on file as a tariff sheet
- Update all tariff sheets to a uniform and standard presentation;
- Remove Rider 1 from Charmar, Cherry Hill, Clarendon, Killarney and Ferson;
- Correct other minor inconsistencies with the tariffs

2. Affiliated Interest and HomeServe USA

Staff's rebuttal testimony raised concerns regarding a marketing agreement between WSC an affiliate of the Companies and HomeServe USA ("Home"). In its surrebuttal testimony, the Companies did not oppose adjustments proposed by Staff to reduce the Companies' revenue requirements by amounts attributable to payments received by its affiliate, Water Services Corp. ("WSC") from HomeServe USA ("Home") as a result of customers enrolling in Home's service repair plans. The Companies also agreed with Staff's recommendation for a proceeding to modify the affiliated interest agreement ("AIA") approved in Docket 08-0335 to address Staff's concerns.

The Companies opposed Staff's recommendation that the Commission find the Companies violated the Public Utilities Act by permitting WSC enter into the marketing agreement with Home. The Companies argued that Staff's recommendation amounted to a misdirected attempt to hold the Companies to the requirement of a provision that has been included in affiliated interest agreements approved by the Commission for other Illinois utilities, but that was not included in the affiliated interest agreement that the Commission had approved for the Companies.

For the purposes of these rate proceedings, the Commission finds that the issues raised by Staff related to the HomeServe transaction have been satisfactorily addressed by the Companies' concessions to reduce their revenue requirements by the amount of HomeServe payments and to participate in a proceeding to address modification of the Affiliated Interest Agreement applicable to all Utility, Inc. affiliates operating in Illinois. Based on hindsight, it appears that it would have been desirable to address Staff's concerns in the docket that approved Companies' affiliated interest agreement. However, the Commission agrees with the Companies that this rate case is not the preferred forum to address those issues, especially since the issues were not raised in response to any direct or rebuttal testimony that the Companies provided in support of their rate proposals. Therefore the Commission declines to approve Staff's proposal to make a finding in this proceeding the Companies have violated the Public Utilities Act.

C. Rules, Regulations, and Conditions of Service Tariffs

Utilities, Inc. witnesses Lena Georgiev and Dimitry Neyzelman proposed updated Rules, Regulations, and Conditions of Service Tariffs for water and/or sewer service for the Utilities, Inc. Companies (Charmar Exhibit 1.0, p. 13; CHWC Exhibit 1.0, p. 12; CWC Exhibit 1.0, p. 12; CWC Exhibit 1.4; KWC Exhibit 1.0, p. 12; KWC Exhibit 1.4; FCUC Exhibit 1.0, p. 12; FCUC Exhibit 1.4; HRUI Exhibit 1.0, p. 13; Exhibit 3.2; and Exhibit 5.2).

Staff witnesses William H. Atwood Jr., William R. Johnson, Thomas Q. Smith, and Jonathan M. Sperry proposed some minor changes to the Companies' proposed Rules, Regulations, and Conditions of Service Tariffs for water and/or sewer service. (ICC Staff Exhibit 6.0, p. 27; ICC Staff Exhibit 7.0, p. 5; ICC Staff Exhibit 8.0, p. 6; ICC Staff Exhibit 13.0, pp. 3-4; ICC Staff Exhibit 14.0, pp. 3-6; ICC Staff Exhibit 15.0, pp. 3-4; and ICC Staff Exhibit 16.0, pp. 5-7)

The Companies agreed with Staff's proposed changes and incorporated them into the proposed Rules, Regulations and Conditions of Service tariffs for water and/or sewer service filed with its Surrebuttal Testimony as Exhibit 5.2. (Exhibit 3.0, pp. 22-24; Exhibit 5.0, p. 3.)

The Commission finds that the Rules, Regulations and Conditions of Service Tariffs for water and/or sewer service identified as Company Exhibit 5.2 are reasonable and should be approved.

D. Additional Accounting Recommendations

Staff witness Ebrey recommended that the Order in this proceeding direct the Companies to: 1) book retirements from plant in service as they occur throughout each year; 2) within 60 days of the final order in these proceedings provide the actual journal entries made to record all retirements addressed and approved herein to the Manager of Accounting and file via e-docket (including those retirements ordered in prior rate cases); 3) within 6-months of final order provide a report to the Manager of Accounting and file the report via e-docket on the Companies' process for identifying the dollar amount to be associated with retirements that takes into account all factors related to the plant to be retired; and 4) complete the plant schedules as well as all other pages of ILCC Form 22 in their entirety and discontinue the shortcut method used in prior years' reports. (Staff Ex. 2.0, pp. 21-22.) The Companies agreed to these recommendations. (Company Ex. 3.0, p.9.) In surrebuttal testimony, the Companies further offered to clarify and analyze its tracking of small projects and retirement processes for small projects and include its finding and recommendations in the report described in 3) above to address the issue of capitalized labor ("cap time"). (Companies Ex. 5.0, p. 7)

E. Rate Shock/Mitigation

1. AG's Position

The Attorney General argues that the proposed rate increases supported by Staff and the Companies would constitute rate shock and violate the ratemaking principle of gradualism. To address the issue of rate shock, AG witness Brosch recommended deferring cost recovery by phasing in rate increases over a period of five to ten years and allowing the Companies receive a return on the-net-of tax regulatory asset balance containing the deferred O&M balance equal to the long term debt interest rate.

2. Staff's Position

Staff recommended that the Commission not adopt an atypical mitigation plan that defers approved rate increases to later periods as proposed by the AG. Under the Attorney General's plan, full recovery of the approved revenue requirement would be delayed for several years from the issuance of the Commission Order in this proceeding, and may result in a level of revenues insufficient to operate and maintain the Companies' water and sewer systems in a safe, adequate and reliable manner. Another problem identified by Staff was such a plan's ability to truly ease the financial burden of higher rates upon customers. In that regard, Staff noted that a customer who defers rate increases pays lower rates today at the cost of much higher rates in the future, particularly because they must pay back all deferred rate increase with interest. Staff also expressed concerns about serious implementation issues that would be necessary to notify and educate customers, modify the billing systems and designing a series of tariffs that would for seven years have an annual anniversary date with revised higher prices. Staff indicated that key components had not been presented by the AG's witness, so that all the details of a phase-in were unable to be properly and adequately

vetted in this docket. Finally, Staff contended that the AG's recommendation will move rates away from the well-established Commission policy of basing rates on cost.

3. Companies' Position

The Companies support the Staff position that the Commission should decline to approve the Attorney General's proposal to phase-in the rates currently necessary to recover the proven costs of providing water and sewer utility services. According to the Companies, the Attorney General's proposal represents an unlawful, fiscally unsound and detrimental policy. Under the Attorney General's proposal, in a future proceeding the Commission could revisit the recovery of the revenue requirement that the Commission had previously found to be just and reasonable. The backward-looking adjustment of rates is equivalent to a reduction of revenues previously approved for a prior period and violates the prohibition against retroactive ratemaking. The Companies further assert the AG's proposal is confiscatory because it would not allow the Companies to recover their cost of capital, which the undisputed evidence in this case shows is 7.98%. To pay for the costs of providing utility services found to be reasonable and necessary, shareholders must advance the cash shortfall that below-cost, phased-in rates would generate. The AG would only allow carrying charges at the below-market rate of 6.65% on the cash working capital provided to fund the shortfall.

The Companies stated that they depend on the rates to meet all the financial obligations to provide service. If the new rates cannot be fully collected, the Companies would be faced with immediate decisions about matters such as where to cut back on system repairs, maintenance, replacements and upgrades needed to maintain service quality and minimize interruptions. Such measures will cause service degradation and increase the costs of bringing the system back to standard at a later time. The Companies expressed the concern that a phase-in plan would increase both the amount and age of unpaid receivables, which will place additional burdens on customers who pay their utility bills. Another flaw cited by the Companies was that phased-in rates by their nature are below the cost of service and below-cost rates encourage inefficient consumption of water and sewer service. In that regard, the Companies maintained that Intergenerational inequities result from charging below-cost rates to current customers resulting in shortfalls that are repaid by future customers so that future customers effectively subsidize consumption by current customers.

The Companies were also opposed to a phase-in proposal because it fails to provide for the recovery of the additional costs that will be incurred to administer the program. The costs for altering the billing system, educating customers about the different billing options and responding to inquiries will divert funds needed to pay other costs of providing utility services, or require further rate relief to continue those services. The Companies urged the Commission not to implement a phase-in plan because it effectively makes "loans" to customers to pay current expenses, which will lead to even higher expenses in future periods. In the future when additional revenue is needed to keep pace with inflation, new regulatory requirements and replacement of aging infrastructure, rate relief will be "pancaked" on top of the deferred recovery of past

costs. Allowing current customers to avoid the reality of the cost to provide utility service provides a temporary false sense of relief that will make rate decisions even more difficult and unpalatable in the future.

The Companies stated that their customer base consists almost entirely of residential customers, so they cannot rely on a commercial and industrial base to provide a revenue stream to finance current operations during a phase-in of rates for residential customers. According to the Companies, the circumstances underlying the Commonwealth Edison ("ComEd") rate moderation plan cited by the Attorney General are not comparable. ComEd has an automatic adjustment rider that enables it to recover increases in uncollectible expenses on a more timely basis than a traditional rate case filing. In addition, ComEd's rates are periodically adjusted to recover its energy costs without filing a rate case.

In the Companies view, the Attorney General's suggestion that the Companies should have filed for rate increases more frequently is not supported by the evidence is short-sighted, unsupported by any case law or Commission decision, and should be rejected as a basis for reducing or postponing the recovery of the Companies' proven costs. The Companies maintain that the record contains no evidence to support a conclusion that more frequent rate cases would have been cost-justified in the past. For example, Charmor had a rate case as recently as 2004, yet as a result of recent developments it needed a large increase in rates to support a major infrastructure replacement, namely the retirement of its well and storage facilities and the need to interconnect its system with a nearby municipal system due to environmental regulations. Several of the other Companies needed rate relief to fund their recently completed or proposed water tank painting and rehabilitation projects. The Companies state they have limited resources to devote to the assembly, submission and defense of the data required to justify rate filings. To file more often would require additional personnel and outside assistance of costly professionals, the costs of which would be borne by customers. The rate case expense for more frequent filings could exceed the amount of revenue increase needed to cover the utility's costs of providing service.

4. Commission Analysis and Conclusions

In our recent order in consolidated Dockets 11-0059, 11-0141 and 11-0142 involving other Illinois subsidiaries of Utilities, Inc., the Commission acknowledged its lack of legal authority to dictate when or how frequently a regulated entity files a case for a rate increase. In that case, we expressed our frustration that those companies had not taken advantage of the Commission's simplified rate procedures under 83 Ill. Admin. Code 255.20(g) for small companies in a more frequent manner if these procedures would have enabled rate increases to occur in more gradual increments and the costs for those cases would have been less expensive. In this way appropriate rate adjustments might have occurred in a manner less dramatic and easier for ratepayers to adjust to and plan for, and, the issue of the costs for water and sewer service would have been brought to the forefront of the public discussion.

Notwithstanding the advantage that hindsight provides regarding the infrequency of past rate filings, the rate increases proposed by Staff are reasonable, supported by the evidence, and should be adopted. While the Commission is mindful that the increases are not small and economic conditions are difficult, the Commission simply cannot deny or postpone a rate increase because the resulting rates are deemed “too high” by one or more parties.

A utility is entitled under the Act to recover its cost of providing utility service and earn a fair rate of return on assets used to provide such service. The record evidence supports the Companies’ and Staff’s position that the Companies’ cannot recover their costs of service under their current rates and that the rates proposed by Staff are necessary for the Companies to recover the costs incurred in meeting their public utility service obligations, including a reasonable rate of return on utility assets. Based on the Commission’s review of the record, both the Companies and Staff considered the financial impact of the rates and made significant efforts to establish rates as low as possible, while ensuring each Company a fair and reasonable rate of return on investments. Unfortunately, for reasons cited by Staff, the Attorney General has not provided any viable solutions to avoid or mitigate any potential rate impact on customers. In summary, there is no legal basis for the Commission to delay a rate increase that reflects the reasonable cost of providing utility service

F. Commission Analysis and Conclusions

The Commission finds the rate design principles, cost-of-service methodologies the development and design of the rates in the manner proposed by Staff and the Staff recommendations described in this section are reasonable. We conclude, therefore, that Staff’s proposals are adopted.

VIII. Findings and Ordering Paragraphs

The Commission, having given due consideration to the entire record herein and being fully advised in the premises, is of the opinion and finds that:

- (1) Charmar, Cherry Hill, Clarendon, Killarney, Ferson and Harbor provide water or water and sewer service within the State of Illinois and, as such, are public utilities within the meaning of the Act;
- (2) the Commission has jurisdiction over the Companies and the subject-matter herein;
- (3) the recitals of fact and conclusion reached in the prefatory portion of this Order are supported by the evidence and are hereby adopted as findings of fact;
- (4) a test year ending September 30, 2010 should be adopted for the purpose of this rate proceeding;

- (5) for the test year ending September 30, 2010 and for the purposes of this proceeding, the rate bases for the Companies are as follows:

| | |
|----------------------|-----------|
| Charmar – Water: | \$295,125 |
| Cherry Hill – Water: | \$498,213 |
| Clarendon – Water: | \$653,767 |
| Killarney – Water: | \$603,588 |
| Ferson – Water: | \$632,085 |
| Ferson – Sewer: | \$63,1969 |
| Harbor – Water: | \$451,925 |
| Harbor – Sewer: | \$65,159 |

- (6) the \$326,456 original cost of water plant for Charmar Water Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant;
- (7) the \$402,961 original cost of water plant for Cherry Hill Water Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant;
- (8) the \$702,376 original cost of water plant for Clarendon Water Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant;
- (9) the \$627,242 original cost of water plant for Killarney Water Co. at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant;
- (10) the \$1,335,221 original cost of water plant for Ferson Creek Utilities Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant;
- (11) the \$1,910,182 original cost of sewer plant for Ferson Creek Utilities Company at December 31, 2009, as reflected on Staff Schedule

10.03, is unconditionally approved as the sewer original costs of plant;

- (12) the \$966,972 original cost of water plant for Harbor Ridge Utilities, Inc. at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant;
- (13) the \$199,135 original cost of sewer plant for Harbor at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the sewer original costs of plant;
- (14) a fair and reasonable rate of return on the Companies' rate bases is 7.98%; this rate of return reflects a fair and reasonable return on common equity of 9.43%; rates should be set to allow the Companies an opportunity to earn that rate of return on its rate base, as determined herein;
- (15) Staff's recommendations with respect to the rate design in this docket should be allowed;
- (16) the Companies' rates, which are presently in effect are insufficient to generate the operating income necessary to permit the Companies to earn a fair and reasonable rate of return and those rates and should be permanently canceled and annulled as of the effective date of the new tariffs allowed in this Order;
- (17) the rates proposed by the Companies in this proceeding would produce rates in excess of that which is fair and reasonable; the Companies' proposed rates should be rejected and the design of the rates in the manner proposed by Staff is reasonable and should be adopted;
- (18) the Companies should be permitted to file new tariff sheets setting forth the rates designed to produce annual operating revenues as follows:

| | |
|----------------------|-----------|
| Charmar – Water: | \$90,250 |
| Cherry Hill – Water: | \$169,812 |
| Clarendon – Water: | \$226,458 |
| Killarney – Water: | \$206,271 |
| Ferson – Water: | \$180,666 |

| | |
|-----------------|-----------|
| Ferson – Sewer: | \$234,582 |
| Harbor – Water | \$141,594 |
| Harbor – Sewer: | \$64,685 |

as such revenues are necessary to provide the Companies a rate of return of 7.98% on their rate bases, consistent with the findings herein; these tariff sheets shall be applicable to service furnished on or after the effective date;

- (19) the rates proposed by Staff that are contained in Section VII hereto are designed in accordance with the rate design determinations made in the prefatory portion of this Order herein above; the Companies should be authorized to file new tariffs setting forth the rates and charges contained in Section VII, effective for all service rendered on and after five (5) business days after filing, with the tariff sheets to be corrected within that time period, if necessary, except as is otherwise required by Section 9-201(b) of the Act as amended;
- (20) the proposed water and sewer depreciation rates by Staff (Identified in ICC Staff Ex. 6.0, Schedules 6.01 CWC, 6.01 KWC, 6.01 FCUC-W, 6.01 HRUI-W, 6.01 FCUC-W and 6.01 HRUI-W) are approved;
- (21) the Companies shall otherwise perform all actions that this Order requires of it;
- (22) the proposed Rules, Regulations, and Conditions of Service tariffs for water and sewer service proposed by Staff and accepted by the Companies are approved
- (23) The Commission finds that the amounts of compensation for attorneys and technical experts to prepare and litigate this proceeding, as adjusted by Staff, are just and reasonable pursuant to Section 9-229 of the Public Utilities Act (220 ILCS 5/9-229); total unamortized rate case expense in the following amounts per Company are approved for recovery:

| | |
|----------------------|-----------|
| Charmar – Water: | \$118,763 |
| Cherry Hill – Water: | \$115,807 |
| Clarendon – Water: | \$115,703 |
| Ferson – Sewer | \$ 56,454 |

| | |
|-------------------|-----------|
| Ferson – Water | \$ 57,664 |
| Harbor – Sewer | \$ 58,106 |
| Harbor – Water | \$ 58,667 |
| Killarney – Water | \$115,398 |

IT IS THEREFORE ORDERED by the Commission that the tariff sheets proposing a general increase in water and sewer rates filed by Charmar, Cherry Hill, Clarendon, Killarney, Ferson and Harbor on June 29, 2011 be, and the same are hereby, permanently canceled and annulled.

IT IS FURTHER ORDERED that the Companies file new tariffs within five (5) business days of the Order, with an effective date of not less than five (5) business days after the date of filing, except as otherwise authorized by Section 9-201(b) of the Act amended, for service rendered on and after their effective date, with individual tariff sheets to be corrected within that time period if necessary. The rates will be in accordance with Findings () and () above and Section ___ herein. Said new tariff sheets shall cancel the tariff sheets presently in effect for, Charmar Water Company, Cherry Hill Water Company, Clarendon Water Company, Killarney Water Co., Ferson Creek Utilities Company and Harbor Ridge Utilities, Inc. with the cancellation date being the same as with the effective date of the new rate tariffs.

IT IS FURTHER ORDERED that the new rate tariffs include provisions for the collection of the Gross Revenue tax (also known as the Public Utility Fund tax) as a separate charge on customers' bills when the rates authorized in this docket go into effect. In conjunction with this change, the following language should be added to the Companies' tariffs:

ANNUAL GROSS REVENUE TAX RECOVERY CHARGE

Section 9-222 of "The Public Utilities Act," as amended, authorizes a utility to recover from its Customers its liabilities to the State of Illinois for Public Utility Annual Gross Revenue Tax imposed by Section 2-202 of "The Public Utilities Act," as amended. Pursuant to Section 9-222, the Company shall charge an Additional Charge for the Public Utility Annual Gross Revenue Tax equal to 0.1 % of all billings under this rate schedule except for (a) this Additional charge for Public Utility Annual Gross Revenue Tax, (b) the Additional Charge for any Municipal Utility Tax, and (c) any other billings and billing items excluded from the base of the Public Utility Annual Gross Revenue Tax.

IT IS FURTHER ORDERED that the \$326,456 original cost of water plant in service for Charmar Water Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$402,961 original cost of water plant in service for Cherry Hill Water Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$702,376 original cost of water plant in service for Clarendon Water Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$627,242 original cost of water plant in service for Killarney Water Co. at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$1,335,221 original cost of water plant in service for Ferson Creek Utilities Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$1,910,182 original cost of sewer plant in service for Ferson Creek Utilities Company at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the sewer original costs of plant.

IT IS FURTHER ORDERED that the \$966,972 original cost of water plant in service for Harbor Ridge Utilities, Inc. at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$199,135 original cost of sewer plant in service for Harbor Ridge Utilities, Inc. at December 31, 2009, as reflected on Staff Schedule 10.03, is unconditionally approved as the sewer original costs of plant.

IT IS FURTHER ORDERED that any petitions, objections or motions made in this proceeding, and not otherwise specifically disposed of herein, are hereby disposed of in a manner consistent with the conclusions contained herein.

IT IS FURTHER ORDERED that, subject to the provisions of Section 10-113 of the Public Utilities Act and 83 Ill. Adm. Code Sec. 200.880, this Order is final; it is not subject to the Administrative Review Law.

By Order of the Commission this ____ day of _____, 2012.

(SIGNED) DOUGLAS P. SCOTT

Chairman